

**NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2003****NOTE 10 – RISK MANAGEMENT**

As a municipal organization, the County has a wide range of loss exposures.

The County uses three internal service funds to account for and finance property/casualty, workers' compensation, and employee medical and dental benefits self-insurance programs. Unemployment liability, excluding that related to Public Transportation and Water Quality Enterprises, is accounted for in the funds with loss experience and as governmental long-term debt. The County contracts with a plan administrator to process medical and dental claims. County fund/claims managers, together with the Civil Division of the King County Prosecuting Attorney's Office, are responsible for processing all tort and workers' compensation claims.

Claims settlements and loss expenses are accrued in the three internal service funds for the estimated settlement value of both reported and unreported claims. These funds are responsible for collecting interfund premiums from insured funds and departments for paying claim settlements and for purchasing certain policies. Interfund premiums are assessed on the basis of claims experience and are reported as revenues and expenses or expenditures.

**Insurance Fund**

The Insurance Fund, an internal service fund, accounts for the County's property/casualty program. The Fund, established in 1977, accounts for the County's exposures to loss due to the tortious conduct of the County, including those commonly covered by general liability, automobile liability, police professional, public officials, errors and omissions, and professional malpractice insurance policies. The estimated liability for probable self-insurance losses (reported and unreported) recorded in the fund at December 31, 2003, is \$41,697,981.

Beginning on July 1, 1993, the County was able to purchase excess liability coverage that provided \$20 million in limits above a \$5 million per occurrence self-insured retention (SIR) for its general liability, automobile liability, police liability, public officials, errors and omissions, and Health Department professional malpractice exposures.

Effective October 1, 1995, the County's excess liability policy was amended to include the exposure of the former Metro government's Transit and Wastewater Treatment functions. The policy limits were increased to \$50 million above a \$5 million per occurrence SIR. Effective August 1, 1997, the County increased limits to \$75 million above a \$5 million per occurrence SIR. Effective September 1, 1998, the County increased limits to \$102.5 million and lowered the SIR to \$2.5 million per occurrence. Effective August 1, 2001, to current, the County decreased the liability limits to \$97.5 million above a \$2.5 per occurrence SIR with an annual \$1 million "corridor" deductible above the \$2.5 million SIR. The County also purchased property insurance that provided a blanket limit of \$3.2 billion with \$240 million in earthquake and \$150 million in flood limits through June 2001.

The event of September 11, 2001, caused property underwriters to pull back on the offering of total insured value blanket limits. FM Global Insurance Company provided a blanket limit of \$500 million in 2002. When the property market began recovering, the County was able to increase overall protection. Effective June 1, 2003, the County renewed the property insurance policy with FM Global Insurance Company. This policy has a blanket limit of \$700 million above a \$100,000 per occurrence deductible. The policy provides an overall

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earthquake sublimit of \$220 million. The 2003 policy was endorsed to cover Certified and Non-Certified Acts of Terrorism on a blanket basis up to \$250 million.

In addition to its property insurance policies and excess liability policy, the County has specific liability insurance policies to cover some of its other exposures. The County has a liability policy for the King County International Airport with policy limits of \$300 million; a property and liability policy to cover the police helicopter activities with liability limits of \$50 million per occurrence; and excess coverage for the Workers' Compensation program over a \$5 million per occurrence SIR. The County also has a combined "crime" coverage policy that provides \$5 million in limits with a \$25,000 deductible. Coverage is provided for protection against loss caused by employee dishonesty; the dishonest acts of third parties in writing or altering checks or other financial instruments; the theft, disappearance and destruction of monies at County locations or when conveyed by a messenger; and for faithful performance of duty.

In the past three years, two occurrences have resulted in payments in excess of the self-insured retention. There have been no settlements in excess of the insurance coverage in the prior three years.

During 2003 there were some significant changes made in the County's insurance program. The County experienced a significant increase in premiums for excess liability insurance from \$3.016 million to \$4.561 million (on an annualized basis) for \$97.5 million in limits. The substantial increase in premium is attributable to our recent large loss experiences (Aurora Bridge and the Solid Waste landfill cases), the substantial tightening in the insurance marketplace and several recent large outcomes within Washington State involving other governmental entities. The County was able to retain a \$2.5 million per occurrence SIR but must satisfy an annual \$1 million "corridor" deductible of \$1 million above the \$2.5 million SIR. (The County must pay an additional \$1 million self-insured retention either from a single large loss or a combination of losses above the County's \$2.5 million deductible.)

The County has increased funding for the self-insurance program commensurate with increases in estimated case reserve requirements and incurred-but-not-reported losses. The cash balance in the Insurance Fund has increased from \$2.1 million at December 31, 1985, to more than \$75 million at December 31, 2003.

In addition to funding reserves for known and incurred-but-not-reported cases, the County has adopted a plan to create catastrophic loss reserves to respond to large losses above the \$1 million limit. The County, by Risk Management policy, retains catastrophic loss reserve balances with interest earnings being invested to the benefit of the catastrophic loss reserve. All County agencies share in financing losses above the \$1 million limit. Through December 31, 2003, \$14.9 million of the \$75 million cash balance in the Insurance Fund has been designated for catastrophic loss reserves (see Note 15, "Restriction, Reserves, Designations, and Changes in Equity").

With the assistance of an actuary, the Insurance Fund's claims liability is estimated based upon historical claims experience and other actuarial techniques. Nonincremental claim adjustment expenses are not included as part of the liability. The changes in the Insurance Fund's claims liability in 2002 and 2003 were as follows:

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	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>End-of-Year Liability</u>
2002	\$ 46,190,229	\$ 3,733,558	\$ (6,676,787)	\$ 43,247,000
2003	43,247,000	9,391,258	(10,940,277)	41,697,981

**Safety and Workers' Compensation Fund**

The Safety and Workers' Compensation Fund, an internal service fund, accounts for the County's self-insurance for workers' compensation as certified under Title 51 RCW, Industrial Insurance Act. Interfund premiums are based on the hours worked by the fund/department-covered employees times an hourly rate that varies for different classes of employees and are recorded as quasi-external interfund transactions. Public Transportation internal fund charges are derived from actuarial projections of their future claims and administrative costs. The estimated liability for probable self-insurance losses (reported and unreported) recorded in the fund at December 31, 2003, is \$16,788,230.

The County purchases an excess workers' compensation policy that provides statutory limits coverage. The amount of loss retained by King County (the self-insured retention) under this policy, effective September 15, 2003, was increased from \$1,000,000 to \$2,000,000. There have been two settlements in excess of the insurance coverage in the prior three years.

The Fund's claims liability is estimated based on reserves for known claims plus a liability for incurred but unreported claims based on historical experience. Changes in the Safety and Workers' Compensation Fund's claims liability in 2002 and 2003 were:

	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>End-of-Year Liability</u>
2002	\$ 12,500,000	\$ 18,134,233	\$ (14,664,233)	\$ 15,970,000
2003	15,970,000	16,772,556	(15,954,326)	16,788,230

**Employee Benefits Program Fund**

The Employee Benefits Program Fund, an internal service fund, accounts for employee medical, dental, vision, life, accidental death and dismemberment, and long-term disability benefit programs, except for Public Safety LEOFF retiree medical benefits. There are five insured and two self-insured medical plans. Seventy-eight percent of County employees are insured through the two self-insured medical plans. The dental and vision plans are also self-insured. Interfund premiums are determined on a per employee, per month basis and charged to departments through a composite rate of expected claims, expenses and premiums. In some cases, there are employee contributions towards premiums. The estimated liability for probable self-insurance losses (reported and unreported) recorded in the fund at December 31, 2003, is \$13,192,000.

The Fund's claims liability is based on historical experience. Changes in the Employee Benefits Program Fund's claims liability in 2002 and 2003 were:

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	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>End-of-Year Liability</u>
2002	\$ 10,761,993	\$ 72,223,017	\$ (71,857,877)	\$ 11,127,133
2003	11,127,133	90,965,941	(88,901,074)	13,192,000

**Unemployment Liability**

The County has elected to retain the risk for unemployment compensation payable to former county employees. The State of Washington Employment Security Department bills the County for the unemployment compensation benefits paid to former employees. Expenditures are then recognized in various county funds. In addition, a long-term liability of \$2,275,000 is recorded in governmental long-term debt for the estimated future claims liability for employees as of December 31, 2003.

Changes in governmental long-term debt liability for unemployment compensation in 2002 and 2003 were:

	<u>Beginning of Year Liability</u>	<u>Current Year Claims and Changes in Estimates</u>	<u>Claim Payments</u>	<u>End-of-Year Liability</u>
2002	\$ 1,172,763	\$ 2,204,171	\$ (1,845,319)	\$ 1,531,615
2003	1,531,615	3,484,358	(2,740,973)	2,275,000

**Component Unit – Harborview Medical Center****Insurance Fund**

Harborview Medical Center (HMC) participates in a self-insurance revolving fund for professional liability coverage through the University of Washington (UW). As of June 30, 2003, the UW did not carry commercial general liability coverage at levels below \$2 million per occurrence. The UW's philosophy with respect to its self-insurance programs is to fully fund its anticipated losses through the establishment of actuarially determined self-insurance reserves. These reserves are deposited in a statutorily created and regulated fund and can only be expended for payment of claim costs and related expenses.

The annual funding to the self-insurance revolving fund is determined by the UW administration based on recommendations from the UW's Risk Management Advisory Committee. The HMC's *pro rata* share of premiums paid to the self-insurance revolving fund were approximately \$1,042,802 in the period July 1, 2001 to June 30, 2002, and \$1,227,665 in the period July 1, 2002 to June 30, 2003.

**Employee Benefits Program**

Eligible permanent employees of HMC receive the basic insurance benefits package that is purchased by the University of Washington through the Public Employees' Benefits Board

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(PEBB). HMC faculty and staff meeting PEBB eligibility rules receive this package of medical, dental, life, and long-term disability (LTD) insurance. In addition, there are optional employee-paid components to the life and LTD that HMC employees may elect.

All employees of HMC are covered by Workers' Compensation and Medical Aid Acts for injuries and occupational diseases that occur during the course of their employment. Coverage includes doctors' services, hospital care, ambulance, appliances, compensations for permanent partial and total disability, and allowances and pensions to surviving spouses and children in the case of fatal injuries. A majority of the premium cost is paid by the UW and a small deduction is made from the employee's pay to conform with the state law.

**Component Unit – WSMILBS Public Facilities District**

The Washington State Major League Baseball Stadium Public Facilities District (PFD) carries commercial general liability insurance with a general aggregate limit of \$2 million and a per occurrence limit of \$1 million. In addition, excess liability coverage is in force at aggregate and per event limits of \$5 million. Business automobile liability coverage limit is at \$1 million per any one accident or loss. Commercial personal property losses are covered up to the replacement value not exceeding \$100,000 with separate overages for earthquake and flood losses.

The PFD also has purchased employee benefit liability coverage with an aggregate limit of \$3 million and a per employee limit of \$1 million.

**Component Unit – Cultural Development Authority of King County**

**Insurance Fund**

The Cultural Development Authority of King County (CDA) carries commercial general liability insurance with a general aggregate limit of \$2 million and a per occurrence limit of \$1 million. Business automobile liability coverage limit is at \$1 million per any one accident or loss. Commercial personal property losses are covered up to the replacement value not exceeding \$103,000.

The CDA also has purchased employee benefit liability coverage with an aggregate limit of \$3 million and a per employee limit of \$1 million.

**Employee Benefits Program**

Employees of the CDA have a comprehensive benefits package through Public Employees' Benefits Board (PEBB). The comprehensive package includes medical, dental, life, and long-term disability coverage. In addition, the PEBB offers the following optional products: long-term care, auto, and home insurance. The State of Washington Health Care Authority (HCA) is the administering authority. The CDA also offers the insurance with American Family Life Assurance Company (AFLAC). With the AFLAC coverage, the CAD employees can pick from a selection of insurance policies.